

RD AN 4181 (4287-B)(4280-B)  
May 4, 2006

SUBJECT: Business and Industry Guaranteed Loan Program  
Liquidation Expenses, Protective Advances, and the Final Report of Loss

TO: State Directors, Rural Development

ATTN: Business Programs Directors

PURPOSE/INTENDED OUTCOME:

The purpose of this Administrative Notice (AN) is to share the findings from a Nationwide Office of Inspector General (OIG) audit on Business and Industry (B&I) loan liquidations and to issue guidance to State Offices regarding authorized protective advances and instances of erroneous and unsupported information of Form RD 449-30, 'Loan Note Guarantee Report of Loss.'

COMPARISON WITH PREVIOUS AN:

This AN replaces RD AN No. 4076 (4287-B) dated April 13, 2005.

IMPLEMENTATION RESPONSIBILITIES:

The OIG audit found that Business Programs personnel had previously authorized ineligible protective advances to lenders that were not entitled to the claim. The claims occurred when the borrowers had voluntarily conveyed collateral securing the loan to the lender in full satisfaction of the debt. The lender then claimed protective advances for expenses incurred in protecting the same collateral. Once the collateral is conveyed directly to the lender, expenses incurred with that property thereafter are liquidation expenses. Protective advances are an indebtedness of the borrower and are secured by the security instruments.

EXPIRATION DATE:  
April 30, 2007

FILING INSTRUCTIONS:  
Preceding RD Instruction 4287-B

Sound judgment must be exercised to determine if the funds expended are a protective advance preserving the recovery of the collateral for the Agency, or if the cost is, an expense of liquidating the collateral. RD Instruction 4287-B, section 4287.156 provides the following: "Protective advances and interest thereon at the note rate will be guaranteed at the same percentage of loss as provided in the Loan Note Guarantee. Protective advances are advances made by the lender for the purpose of preserving and protecting the collateral and constitute an indebtedness of the borrower to the lender. Protective advances must constitute an indebtedness of the borrower to the lender and be secured by security instruments. Agency written authorization is required when cumulative protective advances exceed \$5,000."

In addition, the maximum loss to be paid by the Agency will never exceed the original principal plus accrued interest regardless of any protective advances made. This maximum loss statement should be presented to the lender in writing, once the decision to liquidate is made.

The lender should complete the Final Report of Loss calculations. Some States conduct a final loss audit of the lender's loan ledgers. A final loss audit is recommended, although not required by regulation. RD Instruction 4287-B, section 4287.158 (C ) (4) specifically states: "The lender will show a breakdown of liquidation expenses as to the payee, purpose of the expenditure, date paid, and evidence that the amount expensed was proper and that payment was actually made. *The Agency should review all liquidation expenses to determine if the expenses were proper, reasonable, and in accordance with the approval given by the Agency.* Liquidation expenses are recoverable only from collateral proceeds."

It is the responsibility of Agency personnel to ensure that the Final Report of Loss calculations are correct and justifiable in our role of monitoring and oversight responsibility. In addition, the Agency must complete Appendix B, "Business and Industry Guaranteed Loan Final Loss Settlement Checklist" of RD Instruction 4287-B. Appendix B is a useful tool to assist in determining if the loan was administered as intended; i.e. type of security, source of liquidation proceeds, liquidation costs, etc. Appendix B delineates the loan servicing procedures from the loan's inception to the Final Report of Loss. The documentation compiled from its use provides supportive evidence of the lender's performance of the B&I Guaranteed Loan.

When the lender has not submitted sufficient information to the Agency, or when dollar amounts are in question, State Office personnel should request and review invoices, receipts, cancelled checks, and such documentation required determining if liquidation expenses are reasonable and customary before issuing a final approval of the loss claim.

Please direct any questions to the B&I Division Servicing Branch, (202) 690-4103.

*(Signed by Jackie J. Gleason)*

JACKIE J. GLEASON  
Acting Administrator  
Business and Cooperative Programs